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硕 士 学 位 论 文

当面临腐败问题时, 巴基斯坦的司法系统的品质
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**How Quality of Judicial System in
Pakistan Influence Firms' Decisions when
Faced with Corruption**

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摘要

对商业和制度环境的看法影响了企业家的态度以及他们的商业决策。本文利用来自世界银行企业调查的企业层面的数据，分析了当面对腐败、法律治安情况时，在巴基斯坦企业的决策与法院运作系统的关系。本文认为，缺乏有效的司法体系和有效的监管框架导致了税收征管中猖獗的腐败行为和更高的勒索率。

对企业调查数据的分析表明，巴基斯坦的腐败现象以“收费所”形式出现，通过供水供电的条令出现了“管制俘获”

此外，本文发现在巴基斯坦正式的司法系统不是一个受欢迎的解决纠纷的方式，大多数企业更喜欢另一种机制。本文认为司法系统是商业运作的障碍的认识与征收税收中的腐败显著的正相关。如果企业相信法院系统是公平、高效、负担得起并且有能力强制执行其决议的，他们更可能抵制交钱给 Bhatha 或者将勒索得到的钱财交给黑手党、警察或者政党。

关键词：司法制度；企业家精神；企业决策；税收腐败；Bhatha（勒索）

Abstract

Perception of the business and Institutional environment shapes attitude of entrepreneurs and influence their business decisions. Using the firm level data from the World Bank Enterprise survey, this paper analyzes how decisions of firms in Pakistan are associated with the perception of the functioning of court system, when they face corruption and law and order situations. The paper finds that lack of efficient judicial system and effective regulatory framework leads to rampant corruption in tax collection and higher incidences of extortions. Analysis of the Enterprise survey data shows that corruption in Pakistan occurs in the form of toll booth phenomenon, with regulatory capture taking place through the provisions of water supply and electric power. Moreover, the paper explores that formal judicial system is not a popular resort for dispute resolution in Pakistan, with majority of firms preferring alternative mechanisms. The paper finds positive and significant correlation between the perception of court system being an obstacle for business operations and corruption in tax collection. However, if firms believe that the court system is fair, quick, and affordable and enforce its decisions, they are more likely to resist paying Bhatha (extortion money) to mafia groups, police or political parties.

Key Words: Judicial System; Entrepreneurship; Firms decisions; Tax Corruption; Bhatha (Extortion)

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Chapter 1 Introduction

1.1 Background

The role of institutions in shaping the economy is well acknowledged.¹ “Institutions provide the incentive structure of an economy; as that structure evolves, it shapes the direction of economic change towards growth, stagnation, or decline.” (North 1991) The importance of institutions in improving the economic performances has been thoroughly studied and widely established. Researchers have laid down not only the conceptual framework of the relationship between economic growth and effective institutions, but they are well supported by empirical works. A study by Scully estimated that countries with good institutions are twice as efficient and grow three times as fast in per capita terms as compared to countries with poor institutional endowments (Pinhiero, Armando 1996).

States flourish when different institutions work in harmony for common goal of development and uphold the rule of law, which defines the functioning of these institutions and in return strengthen them. An important institution indispensable to rule of law and economic growth is the judicial system. Judiciary serves to interpret and applies laws and regulations and also provides mechanism for resolution of disputes. It not only serves to protect basic human rights and promote peaceful social relations, but also plays a crucial role in the development of successful market economy.

The legal and judicial system plays significant role in creating an enabling environment for economic development, by shaping the business climate, through protection of property rights, impartial enforcement of contracts, facilitating market activities, maintaining law and order situation, punishing violence and preventing conflicts and extortions. Along with other institutional factors judiciary plays a significant role in creating favorable and thriving environment for businesses and enterprises to flourish.

¹ Douglass C. North, *The Journal of Economic Perspectives*, Vol. 5, No. 1. (Winter, 1991), pp. 97-112.

This paper examines the judicial system of Pakistan and its role in economic development of the country. In particular, the function of courts in enterprise and business development has been explored. Since, perceptions of institutional and business environment shape attitudes of entrepreneurs and influence their business decisions; we analyze that to what extent the functioning of court system and other factors of business environment influence decision of firms in Pakistan. The paper focuses on two different forms of corruption faced by businesses in Pakistan, corruption in tax collection and Extortion, which significantly impact operations of businesses. Since a malfunctioning judicial system is considered to encourage people to behave opportunistically, leading to exploitation, bribery, corruption and extortion, increasing cost for businesses, we explore in this paper that how perceptions of the court system in Pakistan influence the behavior and decisions of firms with regards to corruption and extortions.

Corruption is widespread in Pakistan, observed in different forms including financial and political corruption, bribery, nepotism, misuse of power etc. (Javeed). The recent (2013) report of corruption perception index ranks Pakistan among the most corrupt nation with a score of 28 in the scale of 100. Corruption in various levels of the bureaucracy is regarded as the biggest hurdles by investors in the country (Zakaria 2008). Corruption is considered to be even more pervasive in tax collection, giving a very low Tax-to-GDP ratio of 9%. According to World Bank report (2004) there is a widespread collusion between taxpayers and tax officials which has lead to tax evasion and lack of tax compliance in Pakistan. A recent news report in Express Tribune (April 6, 2014) about the embezzlement of tax income paid by Pakistan Railways, in connivance with officials of Federal Board of Revenue and National bank of Pakistan involving a large sum of money support such claims. Moreover, Tax collection system in Pakistan is considered to be complicated, with more than 37 government agencies, levying more than 70 unique taxes on various goods and services (CNN Feb 11, 2013).

Secondly, corruption in law enforcement agencies such as police and lower judiciary is the major cause of breakdown in law and order situation, leading to

increasing levels of crime (Javeed) and higher incidences of extortion, known as Bhatha in local context. Bhatha is terror tax or informal protection money collected by police, political parties or mafia groups from businesses in return for their kind of protection (i.e. they will not cause harm to the establishment if they are paid protection money). In Karachi alone, which contribute to 25% of the GDP of the country, 1300 extortion cases were registered in the year 2013, with hundreds other unreported (world news). Rampant and widespread corruption among different institutions of the country and higher incidences of extortion in Pakistan, with different actors involved such as public officials, politicians, and police and mafia groups appears to follow the toll booth phenomenon which implies that “corruption is often considered as the ‘only way to keep a business going’ faced with ‘unfair’ or ‘inefficient’ laws and regulations” (Boehm 2007). This paper also tries to find out the various aspects of the institutional environment or different agencies which contribute to the toll booth process of corruption in Pakistan. In addition, this paper also summarizes relevant literature on the functioning and performance of judicial system in Pakistan.

Summarizing the objectives of this paper, it serves the following purposes: first, to examine the functioning and performance of court system in Pakistan on the basis of available literature, secondly, to find the association of perception of judicial system in Pakistan to different kinds and level of corruption faced by enterprises, and how the perception of court system shapes firms’ decisions.

We employ firm level data from the World Bank enterprise survey to see the correlation firms’ decisions with the perception of entrepreneurs about the functioning of court system and other aspects of the institutional environment. The main findings of this paper can be summarized as follows. When entrepreneurs in Pakistan believe that judicial system is fair, quick, affordable and able to enforce its decisions, they are less likely to pay ²Bhatha (an informal payment) or “terror tax” to political parties or mafia groups for the sake of protection. Payment of Bhatha is also significantly correlated with the level of corruption being an obstacle for business operations.

²Bhatha is a term commonly known for extortion in Pakistan which is collected by political parties or mafia group in the name of protection

Secondly, regression outcome shows that corruption and bribery in tax payment is positively and significantly related with the perception of court system being inefficient. The results in this study are based on the cross-sectional data obtained from Enterprise survey period 2007. Although panel data would have given more robust results on the marginal effects of the variables, but some missing values from the previous survey limit us to the data of 2007.

The paper's structure is as follows. Section 2 of chapter 1 reviews the literature on the role of judicial system in controlling corruption and fostering economic development. Chapter 2 gives an overview of judicial system of Pakistan and its influence on the attitudes of individuals and entrepreneurs. In Chapter 2 we also discuss the prevalence of tax corruption and Bhatha or Extortion in Pakistan. Chapter 3 presents the data and methodology. Chapter 4 discusses the empirical results and Chapter 5 concludes.

1.2 Literature Review

According to Stopler (2006) an important function of the court system is to ensure the rule of law which encourages entrepreneurship and business development. An effective judicial system increases people's confidence on the legal system and encourage them to organize their economic activities accordingly, promote the comprehension and exercise of legal approaches, ensure protection of property and rights, and advocate proper compensation (Pinhero Armando 1996). Moreover, it verifies and strengthens property rights, enforce contracts and agreements, streamline businesses and provide legal security for economic transactions. Hence it helps create an environment of trust encouraging people to invest in their assets, trade freely, take risks, and ultimately contributing to the economic growth of the country. (Kevin, Fandle). On the other hand, a malfunctioning judicial system will encourage people to behave opportunistically, leading to exploitation, bribery and corruption, hence increasing the cost for businesses. "A poor justice system may encourage the development of corruption which incurs extra financial costs (i.e. rise of transaction

costs) for entrepreneurs and slows business down” (EC 2013). Business costs will increase because people have to pay bribe in order to survive.

Shleifer and Vishny (1998) found that corruption raises costs both for producers and consumers by diverting resources into rent-seeking behavior and bribery. According to Sullivan and Shkolnikov (2005), the quality of legal and judicial system can have significant impact on the pervasiveness of bribery, by influencing the decisions of enterprises when they face demand for unofficial payments. Affective judiciaries increase the cost for corrupt deals whereas if the judicial system is malfunctioning, the incentives for corrupt behavior will outweigh the costs, reducing the risk of extortions and bribery (Susan Rose 2010).

Failure of the court system to work efficiently provide the public officials and politicians an opportunity for corruption and rent-seeking, which affects the level of investment and entrepreneurial incentives (Arvind 2001). Kaufmann (1997) explored that the fear of extortions and misappropriation impede long-term foreign and domestic investments, misallocate talents to rent-seeking activities, and push firms to operate outside the formal sector, thus leading to tax evasion and denying the state of revenue to spend on public expenditures.

Haggard (2011) summing up the literature on the rule of law and its impact on economic growth describes that absence of strong legal and judicial system can leads to extortion, predation, violence, anarchy, civil conflicts and hamper economic growth. According to Sullivan and Shkolnikov, “corruption prospers in countries with weak legal systems, poor enforcement mechanisms, vague and complex laws and regulations, and too much discretionary power with little transparency at various levels of government”.

Judicial system has an important role in curbing corruption and crime by maintaining law and order situation, upholding the rule of law, punish violations and hence, providing an enabling environment for businesses to flourish. Effective judicial system ensures provision of security of property and protection of economic agents themselves (Haggard and Tiede 2010). According to Haggard (2011), that of the various dimensions of the rule of law, the basic control of violence has the strongest

correlation to economic growth in developing countries. Strong judiciaries ensure the provisions of law and order by increasing the deterrence effect of laws by punishing crime, fraud, extortions, violence and other law violations. On the other hand, “slower judiciaries lower the discounted value of punishment, thereby weakening incentives to act in accordance to laws” (Chemin 2007).

Herare, Lijane and Rodriguez (2007), found that incidences of corruption could be reduced by increasing access to the judicial system and by investing on its efficacy. Matthieu Chenmin (2007) while evaluating the Pakistan’s Access to Justice Program (2002-2003) proved that finding ways to speed up judiciaries is fundamental for economic growth. Using a difference-in-difference approach, he showed after the implementation of judicial reforms, judges disposed 25% more cases, which improved the law and order situation in the affected districts creating favorable conditions for spurring entrepreneurship, increasing trust on formal institutions and access to finance leading to increase in employment and employment opportunities.

However, according to Jean, Maximilia and Stephane (2010) “if social order and control is weak, firms have to invest heavily in defensive measures such as private security”. High costs of litigations and prolong time, added with politicized judgments and corruption in law enforcement hamper firms operating in such environment from utilizing their resources efficiently, failing to achieve their potential output and discouraging them to expand in the long terms. As a result firms would prefer to operate in an unofficial sector, avoid economic activities that might require court help, paying for private protection and contract enforcement instead of official taxes (Chemin 2007, Jaswant). This explains why firms and enterprises cooperate with extortionists, paying them extortion money and ensuring protection of their properties, in countries with weak legal regimes. Weak legal and regulatory framework causes entrepreneurs to behave opportunistically in connivance with corrupt officials of public departments, a phenomenon explored by capture and toll booth theories. According to tollbooth theory, if regulations are inefficient, they serve to create and extract rents for politicians and bureaucrats. And stability of regulatory framework is an important factor influencing firms’ decisions when it comes to make

investment especially for foreign firms. Capture theory emphasize benefits to the firms as a result of rent creation and extractions (Djankov 2002). This paper will also test for toll booth theory in the business environment of Pakistan that which particular aspects are prone to extractions by public officials or politicians due to corruption and weak regulatory frameworks.

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Chapter2 The Context of Pakistan: Judicial System, Corruption and Bhatha

In this section we will talk about brief history, structure and performance of the judicial system of Pakistan and how it has influenced the behavior of individuals and enterprises. This section also discusses prevalence of Corruption and incidences of Bhatha in Pakistan, to get insight into the adversity of the situation. Moreover, we will also include statistics from the Enterprise survey on functioning of court system, tax corruption and Extortion.

2.1 Judicial System in Pakistan

After partition of the Indian subcontinent, the Government of India Act 1935 was retained as the provisional constitution of newly established Pakistan, with slight modifications. So the basic legal and judicial structure has been derived from the British Model or the common Law system. The subsequent constitutions of Pakistan, 1956, 1962 and 1973 brought only few development to the judicial structure which included establishment of federal court for Pakistan which was later named as the Supreme Court, institutions of full-fledged high courts in the province of Baluchistan and KPK (then NWFP) and inception of Federal Shariat Court in 1980 (Faqr Hussain 2011).

According to Article 175 (article establishment and jurisdiction of courts) of the constitution of Pakistan,³ “There shall be a supreme court of Pakistan, a High court for each province; a high court for Islamabad territory and such other courts as may be established by laws”. So the judicial system of Pakistan consists of⁴(Justice Tanvir):

(a) Superior judiciary comprising of Supreme Court, Federal Shariat Court and High Courts.

³ Part VII, The Constitution of Pakistan (<http://www.pakistani.org/pakistan/constitution/part7.ch1.html>)

⁴Judicial system of Pakistan by Justice (R) Tanvir Ahmed Khan

(b) District judiciary comprising of civil and Criminal Courts created by acts working under the supervision and control of the respective High Courts under Article 203 of the Constitution.

(c) The Administrative Courts, Tribunal, and special courts created under different laws.

Special Courts, which normally work under the ministry of law and justice include courts for Control of Narcotics Substances, Banking Courts (Recovery Loans and Offences in Banks), Customs, Taxation & Anti-Smuggling, Income Tax Appellate Tribunal, Environment Appellate Tribunal, Insurance Appellate Tribunal, Customs, Excise & Sales Tax Appellate Tribunal, Special Judges (Central), Drugs Courts, Anti-Terrorism Courts, Accountability Courts (Faqr Hussain:22).

According to the constitution of 1973, superior courts including the supreme court and high courts are authorized to judicially review legislation as well as executive action and ensure the enforcement of fundamental rights(USAID: 2008). But the superior courts and particularly, the Supreme Court has never been truly independent with its history dwelling with controversial decision, including the validation of various military takeovers, abrogation of constitutions and various extra-constitutional steps of the executive branch. The ⁵Moulvi Tamizudding Case (1955), ⁶Dosso Case (1958), ⁷Nusrat Bhutto case (1977) and ⁸Zafar Ali shah case (2000), in which the Supreme Court validated the military take over all tell the same story – politicization, corruption and compromise of the rule of law on the hand of the same

⁵In 1954, Governor General Ghulam Muhammad dissolved the Constituent Assembly. Maulvi Tameezuddin challenged this decision in the Sind High Court. Sind High Court decided the case in his favor. But when Federal Government appealed against the decision in the apex court, Chief Justice Munir declared the verdict of Sind High Court null and void and invoked the notorious and highly controversial ‘doctrine of necessity’. This turned out to be the precedent for subsequent undemocratic actions whenever the army generals took over the reins of the country. The role of the judiciary also proved to be a confederate in the process of subverting the democratic systems. - See more at: <http://storyofpakistan.com/maulvi-tamizuddin/#sthash.Hm9sBWuG.dpuf>

⁶in case of State v.Dosso (PLD 1958 SC (Pak) 533) validated the imposition of martial law by invoking the Kelsenian theory and held that, “a victorious revolution was itself a law creating fact.” Constitution History of Pakistan (<http://www.zklawassociates.com/wp-content/uploads/2012/03/CONSTITUTIONAL-HISTORY1.pdf>)

⁷ In 1977, after imposition of Martial Law in the country, the Constitution was held in abeyance and replaced by an interim Provisional Constitutional Order (PCO). In the Nusrat Bhutto case (1977) the Supreme Court once again validated the coup on the basis of the Common Law “doctrine of state necessity.” Constitution History of Pakistan (<http://www.zklawassociates.com/wp-content/uploads/2012/03/CONSTITUTIONAL-HISTORY1.pdf>)

⁸In 1999 after the military takeover of Pervez Musharraf, Proclamation of Emergency was declared, the constitution was put in abeyance, a Provisional Constitutional Order (PCO) was issued to provide a temporary governing framework and a reconstituted Supreme Court decided the case of Zafar Ali Shah v General Pervez Musharraf (PLD 2000 SC 869) 2000) and validated the coup on the grounds of the doctrine of state necessity

body which is entrusted with its safeguard. Apart from these there are several other instances of politicized judgments of the judiciaries in Pakistan which have compromised integrity of the justice system. And it's argued that the long spells of military rule has considerably contributed to the underdevelopment of Pakistani justice system.

An important observation has been made by USAID in its assessment of rule of law in Pakistan. According to this study, legitimacy is the basic issue of the Pakistan's current body of law and legal systems which is a product of four main historical forces: British Colonial system, democratic law making, Military rule and Shariah and the interaction of these forces contributed to a perception of the Pakistan legal framework as confusing, inconsistent and incoherent (USAID 2008: 9). "In addition, the progressive weakness of the state bureaucracy and the judicial processes since the independence of the country has created greater space, and some may argue need, for community-based adjudication and dispute resolution through local and tribal councils (variously composed according to local customs and referred to as Jirgas, Panchayats, etc. in different parts of the country)" (USAID 2008). Together, all these have created a complex situation which hampers justice rather than ensuring it.

Siddique has painted a very bleak picture of the legal and judicial system of Pakistan in his article. According to him, "it is slow, expensive, vulnerable to exploitation and misuse, coercive, unintelligible to the majority due to its complexity, made further inaccessible due to poor regulation of the legal profession and resilient to reform" (Siddique 2011). He argues that such an unreliable, slow and venal justice system, encourage disgruntled people to resort to parallel alternatives and it was the reason for popularity enjoyed by the Taliban brand of governance in the Swat valley who had promised a speedy justice system (Siddique 2011).

A number of studies on the Pakistan judicial system agree that it suffers from lengthy case delays and high pendency rates (USAID assessment, AJP program of ADB, Siddique, Hussain). A study by Asian development Bank confirmed that it takes 118 months on average to decide civil disputes. According to business Climate and legal and Institutional reform study, real property disputes which make up 75-90% of

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